

**PUBLIC**

10 AUG 1994

RESPONSE OF THE OFFICE OF CHIEF COUNSEL  
DIVISION OF INVESTMENT MANAGEMENT

Our Ref. No. 93-372-CC  
W.R. Huff Asset  
Management Co., L.P.  
File No. 801-32541

Your letter of May 26, 1994 requests our assurance that we would not recommend enforcement action to the Commission under the Investment Advisers Act of 1940 ("Advisers Act") if W.R. Huff Asset Management Co., L.P. ("WRH"), a registered investment adviser, does not treat certain of its limited partners as advisory representatives for purposes of the recordkeeping requirements of Rule 204-2(a)(12) under the Advisers Act. 1/

WRH is a Delaware limited partnership with two general partners, two limited partners who are also employees of WRH, and five individual limited partners each of whom owns, holds, or controls less than five percent of WRH's limited partnership interests ("Outside Limited Partners"). You state that the Outside Limited Partners are passive investors; they do not participate in formulating investment decisions for WRH's advisory clients and do not receive any advance information regarding WRH's investment decisions or securities transactions for clients. The Outside Limited Partners' access to WRH's offices has been, and will continue to be, strictly limited. Although one Outside Limited Partner and relatives of two Outside Limited Partners are WRH advisory clients, you state that WRH has full investment discretion to trade securities on behalf of these (and all of its) advisory clients, and that clients receive no advance information regarding proposed purchases or sales of any securities. 2/

Rule 204-2(a)(12) requires each registered investment adviser to maintain records of securities transactions of its advisory representatives, which the rule defines to include "any

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1/ With certain exceptions not relevant here, Rule 204-2(a)(12) requires registered investment advisers to maintain records of every transaction in securities in which the adviser or any advisory representative thereof has or acquires a direct or indirect beneficial interest.

2/ One Outside Limited Partner reviews WRH's general ledger quarterly for all Outside Limited Partners. The ledger contains WRH's financial records and a list of advisory clients, but does not include any information about securities held in client portfolios or transactions effected or to be effected for clients.

partner" of the adviser. 3/ The Commission adopted Rule 204-2(a)(12) as a means of preventing "scalping" which it described as a practice "whereby an investment adviser, or any person who obtains information concerning a securities recommendation being made by such investment adviser prior to the dissemination of such information, trades on the anticipated short-run market activity which may ensue from the issuance by the adviser of the securities recommendations." 4/

You state that the Outside Limited Partners are analogous to an incorporated investment adviser's non-controlling shareholders, who are not included within the definition of advisory representative unless they also have another relationship with the adviser that is specified in the rule. Because the Outside Limited Partners have no other relationship with WRH, and do not receive or have access to advance information about WRH's investment decisions or trading activities, you believe that it would be consistent with the purposes of the rule to treat the Outside Limited Partners like their shareholder counterparts and not require WRH to maintain records of their securities transactions. 5/

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3/ Other persons included within the definition of "advisory representative" include the adviser's directors and officers, and those employees who participate in making investment recommendations or obtain information about investment recommendations prior to the effective dissemination thereof; and any of the following persons who obtain information concerning securities recommendations prior to the effective dissemination thereof: (i) persons in a control relationship to the adviser, (ii) any affiliated person of such control person, and (iii) any affiliated person of such affiliated person.

4/ See Investment Advisers Act Release Nos. 203 (Aug. 11, 1966) and 436 (Feb. 14, 1975) (releases adopting and amending Rule 204-2(a)(12)). We note that the rule was intended to address other conflicts of interests in addition to scalping. See American Syndicate Advisors (pub. avail. Sept. 29, 1986) and Cortland Financial Group, Inc. (pub. avail. Sept. 26, 1985) (no-action relief denied notwithstanding the unlikelihood of scalping because records potentially could reveal soft dollar arrangements or other brokerage practices that might create a conflict of interest).

5/ You also state that relief is appropriate because there is little practical risk of scalping in the high yield bond market (in which WRH specializes) because (1) the price of these securities generally does not fluctuate much, and (2)

You also point out that the Commission recently sought to equalize the treatment of limited partners and shareholders under the Investment Company Act of 1940 ("1940 Act"), recognizing that they are similarly situated. Section 2(a)(3)(D) of the 1940 Act defines affiliated person to include any "partner" of another person. The Commission recently adopted Rule 2a3-1 under the 1940 Act to except limited partners from this definition if the sole reason for the affiliation arises from being a limited partner investor. 6/ We are persuaded that the same reasoning underlying the adoption of Rule 2a3-1 applies in the circumstances you describe.

Accordingly, on the basis of the facts and representations in your letter, we would not recommend enforcement action to the Commission under Rule 204-2(a)(12) if WRH does not maintain records of the Outside Limited Partners' securities transactions. This response expresses the Division's position on enforcement action only and does not purport to express any legal conclusions on the issues presented.

*Barbara Chretien-Dar* <sup>FMAD</sup>  
Barbara Chretien-Dar  
Senior Counsel

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the Outside Limited Partners cannot participate in the high yield bond market because the securities often are restricted in accordance with Rule 144A under the Securities Act of 1933. We disagree. While high yield bonds may be less susceptible to scalping than other types of securities, the potential for abuse still exists. The prices of these securities can be highly volatile and may fluctuate in response to sizeable purchases and sales.

6/ See Investment Company Act Release No. 19658 (Aug. 25, 1993). The rule does not provide an exception for a limited partner of an investment company that is affiliated by virtue of any other relationship described in Section 2(a)(3), such as a 5 percent or greater ownership stake in the company.

SULLIVAN & CROMWELL

Investment Advisers Act of 1940  
Rule 204-2(a)(12)

NEW YORK TELEPHONE: (212) 558-4000  
TELEX: 62694 (INTERNATIONAL) 127816 (DOMESTIC)  
CABLE ADDRESS: LADYCOURT, NEW YORK  
FACSIMILE: (212) 558-3586 (125 BROAD STREET)  
(212) 558-3792 (250 PARK AVENUE)

*125 Broad Street, New York 10004-2498*

250 PARK AVENUE, NEW YORK 10177-0021  
1701 PENNSYLVANIA AVE., N.W., WASHINGTON, D.C. 20006-5805  
444 SOUTH FLOWER STREET, LOS ANGELES 90071-2901  
8, PLACE VENDÔME, 75001 PARIS  
ST. OLAVE'S HOUSE, 91 IRONMONGER LANE, LONDON EC2V 8EY  
101 COLLINS STREET, MELBOURNE 3000  
2-1, MARUNOUCHI 1-CHOME, CHIYODA-KU, TOKYO 100  
3602 GLOUCESTER TOWER, 11 PEDDER STREET, HONG KONG

May 26, 1994

By Hand

Office of the Chief Counsel,  
Division of Investment Management,  
Securities and Exchange Commission,  
450 Fifth Street, N.W.  
Washington, D.C. 20549.

ACT IAA  
SECTION             
RULE 204-2(a)(12)  
PUBLIC AVAILABILITY 8-10-94

Re: W.R. Huff Asset Management Co., L.P.

Dear Sirs:

On behalf of our client W.R. Huff Asset Management Co., L.P., a Delaware limited partnership ("WRH"), and on behalf of any persons that may from time to time be limited partners of WRH, we hereby respectfully request that the staff (the "Staff") of the Securities and Exchange Commission (the "Commission") confirm to us that, based on the facts set forth in this letter, certain limited partners of WRH that own, hold or control less than five percent of the outstanding limited partner interests of WRH should not be treated as "advisory representatives" pursuant to Rule 204-2(a)(12) under the Investment Advisers Act of 1940, as amended (the "Act"), and that therefore the Staff would not recommend enforcement action to the Commission if WRH does not maintain the records of securities transactions of such

limited partners as is required for the securities transactions of advisory representatives pursuant to Rule 204-2(a)(12).

I. Background Information

WRH is currently one of the leading managers of high yield debt securities in the United States and is registered as an investment adviser under the Act with its principal place of business at 30 Schuyler Place, Morristown, New Jersey. WRH is a limited partnership with two general partners (the "General Partners") including Mr. William R. Huff, two limited partners who are also employees of WRH with an aggregate partnership interest of less than nine percent (the "Employee Limited Partners")\* and five individuals who each own a limited partnership interest of less than five percent (the "Outside Limited Partners" and, together with the Employee Limited Partners, the "Limited Partners"). WRH is the successor to a New York limited partnership organized in 1984. In 1984, the Outside Limited Partners were brought in to provide capital to fund the operations of WRH until WRH became self-supporting. Three

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\* One of the two Employee Limited Partners will retire this year, after which WRH will treat him as an Outside Limited Partner, and WRH undertakes that all of its undertakings with respect to the other Outside Limited Partners will apply to the Employee Limited Partner upon his retirement.

of the Outside Limited Partners, one of whom is currently the Reviewing Limited Partner (as defined below), had an existing business relationship with Mr. Huff. These three Outside Limited Partners in turn brought in the remaining Outside Limited Partners (the "Additional Outside Limited Partners"). None of the General Partners, Employee Limited Partners or staff of WRH has or has ever had any personal, social or business relationship, nor has ever even met or spoken with, these Additional Outside Limited Partners.

The Outside Limited Partners of WRH are entirely passive investors. According to the terms of the Agreement of Limited Partnership governing WRH, the General Partners have the exclusive right to manage the business of the partnership to the complete exclusion of the Limited Partners. In fact, the Outside Limited Partners have never participated in the management of WRH in any respect and, in particular, have not participated in the formulation of investment decisions to buy or sell securities on behalf of WRH's investment management clients and have not obtained information (either in advance or after the fact) concerning WRH's investment decisions or trading activities (including any transaction reports or client account statements). As a condition of the relief requested hereby, WRH will undertake to continue to exclude the Outside Limited Partners from the

process of formulating and executing WRH's securities investment decisions and from receiving any client information.

One of the Outside Limited Partners (the "Reviewing Limited Partner") receives WRH's general ledger for review on a quarterly basis on behalf of the other Outside Limited Partners. This ledger contains WRH's financial records and also includes a list of its investment management clients and the fees received from each such client, but contains no information concerning securities held in the clients' portfolios or the securities trading activities conducted on behalf of WRH's clients.

The Reviewing Limited Partner came to fulfill that function not by any explicit written agreement, but rather for practical reasons: (i) the Reviewing Limited Partner was principally responsible for bringing in as Limited Partners the Additional Outside Limited Partners, (ii) the Reviewing Limited Partner had prior business relationships with both Mr. Huff and the Additional Outside Limited Partners and (iii) the Reviewing Limited Partner is a certified public accountant ("CPA") and therefore qualified to review WRH's general ledger.

WRH understands that the Reviewing Limited Partner no longer personally reviews the general ledger. Instead,

he refers the general ledger to another CPA (the "Independent CPA") for such review. The Outside Limited Partners pay the Independent CPA for their pro rata share of her fees.

The Outside Limited Partners (other than the Reviewing Limited Partner) do not receive the general ledger or any summary, excerpt or other report thereof of any kind. They receive only their quarterly distributions of profits from WRH's operations. As a condition to the relief requested hereby, WRH will undertake to continue to provide the Reviewing Limited Partner with only the type of information he has previously received; the other Outside Limited Partners will continue to receive only their quarterly distributions of profits.

One of the Outside Limited Partners and relatives of two of the Outside Limited Partners are also WRH clients. As with WRH's other clients, the investment management agreements with these clients provide that WRH has full investment discretion and authority with respect to the trading of securities in their respective accounts. These clients receive monthly statements which list the securities owned in their respective accounts, their cost basis and current market prices. These clients are not consulted prior to the purchase or disposition of any security, nor

are they provided with information concerning such transactions prior to their effective execution. As a condition of the relief requested hereby, WRH will undertake to continue to provide these clients with no more than the type of information they have previously received.

## II. Discussion

### A. Relief Requested

Absent the relief sought herein, pursuant to Rule 204-2(a)(12)(A) of the Act, the Outside Limited Partners would be deemed to be "advisory representatives" solely because they are limited partners. An advisory representative may engage in transactions in securities in which such advisory representative has, or by reason of such transaction acquires, a direct or indirect beneficial ownership ("Securities Transactions"). Pursuant to Rule 204-2(a)(12) of the Act, an investment adviser is required to maintain records of Securities Transactions of its advisory representatives unless the transactions are effected in accounts over which neither the adviser nor any advisory representative has any direct or indirect influence or control or the transactions are in securities which are direct obligations of the United States (all Securities Transactions other than such excepted transactions, the "Personal Securities Transactions").

We believe that the definition of advisory representative in Rule 204-2(a)(12) should be interpreted to exclude the Outside Limited Partners of WRH. We do not believe that requiring WRH to maintain records of all of the Outside Limited Partners' Personal Securities Transactions would further the underlying purposes of Rule 204-2(a)(12). On behalf of our client WRH, we request that the Staff confirm to us that the Outside Limited Partners should not be treated as "advisory representatives" pursuant to Rule 204-2(a)(12) under the Act, and that therefore the Staff would not recommend enforcement action to the Commission if WRH does not maintain the records of Personal Securities Transactions of such Outside Limited Partners as is required for the Personal Securities Transactions of advisory representatives pursuant to Rule 204-2(a)(12).

WRH has in the past and will continue in the future to maintain the records required pursuant to Rule 204-2(a)(12) with respect to the Personal Securities Transactions of the General Partners and the Employee Limited Partners. The relief requested herein would apply only to the Outside Limited Partners. In addition, WRH will undertake to continue to exclude the Outside Limited Partners from the process of formulating and executing WRH's

investment decisions and trading activities and from receiving any information related thereto.

B. Rule 204-2(a)(12)

Rule 204-2(a)(12) of the Act requires that all advisers maintain a record of every Personal Securities Transaction of the investment adviser or of any advisory representative of such investment adviser.

Rule 204-2(a)(12)(A) defines advisory representative to include (1) any partner, officer or director of the investment adviser; (2) any employee who makes any recommendation, who participates in the determination of which recommendation shall be made, or whose functions or duties relate to the determination of which recommendation shall be made; (3) any employee who, in connection with his duties, obtains any information concerning which securities are being recommended prior to the effective dissemination of such recommendations or of the information concerning such recommendations; and (4) any control person of the investment adviser or any affiliated person of such control person who obtains information concerning securities recommendations being made by such investment adviser prior to the effective dissemination of such recommendations or of the information concerning such recommendations.

Absent the relief sought herein, the Outside Limited Partners would be deemed advisory representatives of WRH for no other reason than because they are limited partners of WRH. WRH would therefore be required to maintain records of the Outside Limited Partners' Personal Securities Transactions. The Outside Limited Partners do not fall within the definition of advisory representative under Rule 204-2(a)(12)(A) in any other respect.

C. Analysis of Rule 204-2(a)(12)

Rule 204-2(a)(12) was adopted pursuant to the authority granted the Commission in Sections 204, 206(4) and 211(a) of the Act. Generally, Section 204 of the Act requires every investment adviser to make, keep and preserve for such periods, such records and reports as the Commission by its rules and regulations may prescribe as necessary or appropriate in the public interest or for the protection of investors. Section 206(4) prohibits any investment adviser from engaging in any act, practice, or course of business which is fraudulent, deceptive or manipulative and gives the Commission the authority, by rules and regulations, to define and prescribe means reasonably designed to prevent such fraudulent, deceptive and manipulative acts, practices and courses of business. Section 211(a) gives the Commission authority to make, issue, amend and rescind such

rules and regulations as are necessary or appropriate to the exercise of the functions and powers conferred upon it under the Act.

Rule 204-2(a)(12) was adopted in order to "assist the Commission in determining whether a further rule to prohibit scalping is necessary...." Adoption of Amendment to Rule 204-2, Investment Advisers Act Release No. 203, [1966-1967 Transfer Binder] Fed.Sec.L.Rep. (CCH) ¶ 77,401, at 82,712 (Aug. 11, 1966). "Scalping," as defined by the Commission in a release which amended Rule 204-2(a)(12) and adopted Rule 204-2(a)(13) in 1975, "is a practice whereby an investment adviser, or any person who obtains information concerning a securities recommendation being made by such investment adviser prior to the dissemination of such information, trades on the anticipated short-run market activity which may ensue from the issuance by the advisor of the securities recommendation."\* Investment Advisers Act Release No. 436 (the "Amending Release"), [1974-1975 Transfer Binder] Fed.Sec.L.Rep. (CCH) ¶ 80,113, at 85,116-17 (Feb. 29, 1975). The Commission also stated in the Amending Release that Rule 204-2(a)(12) has

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\* The United States Supreme Court, in S.E.C. v. Capital Gains Research Bureau, Inc., 375 U.S. 180 (1963), found scalping to be a fraudulent and deceptive practice within the meaning of Section 206 of the Act.

served as a deterrent to the practice of scalping since it requires all advisory representatives (i.e., persons who may have information concerning advisory recommendations prior to dissemination) to report all of their securities transactions to their affiliated advisory firms on a regular basis. These reports are, moreover, subject to examination by representatives of the Commission. It is necessary and important, therefore, that records of securities transactions be maintained for all persons who obtain information concerning advisory recommendations prior to the issuance and dissemination of such recommendations.

Amending Release at 85,117.

As indicated in the Amending Release, the Commission views sub-paragraphs (12) and (13) of Rule 204-2(a) as complementary with their primary purpose being to prevent scalping on the basis of information concerning securities recommendations made available to advisory representatives prior to the effective dissemination of such information. The Commission stated that since information effectively disseminated to advisory clients and other intended users "is no longer suitable as a basis for engaging in scalping," it is not necessary for an adviser to maintain records of securities transactions of persons who receive information concerning a securities recommendation only contemporaneous with or subsequent to the effective dissemination of such information. To clarify these points, the Amending Release amended Rule 204-2(a)(12) and added Rule 204-2(a)(13). The amendment to Rule 204-2(a)(12)

carved out from the definition of "advisory representative" those employees, controlling persons of investment advisers, affiliated persons of such controlling persons or affiliated persons of such affiliated persons who obtain information with respect to the investment adviser's securities recommendations after the effective dissemination of such information.

Rule 204-2(a)(13) of the Act prescribes the same record keeping requirements for Personal Securities Transactions of investment advisers and advisory representatives "where the investment adviser is primarily engaged in a business or businesses other than advising registered investment companies or other advisory clients." Rule 204-2(a)(13), however, limits the record-keeping requirements in the case of partners, officers and directors, as well as employees, controlling persons and affiliates, to those persons who have some relationship to the investment advisory business performed by the registered investment adviser or who obtain information concerning investment recommendations prior to the effective dissemination of such information.

In conformity with the Commission's policy in adopting Rule 204-2(a)(12), the relief requested hereby is grounded on the Outside Limited Partners' actual lack of

access to information concerning investment decisions or trading activities of WRH and the resultant lack of risk of scalping by them. As was noted above, the Outside Limited Partners of WRH are entirely passive investors: (i) they have not, do not and cannot participate in management nor in the formulations of investment decisions to buy or sell securities on behalf of WRH's investment management clients and (ii) each holds less than five percent of the total partners' capital of WRH. Furthermore, there is no issue as to the Outside Limited Partners obtaining information concerning WRH's investment decisions and trading activities prior to the effective dissemination of such information; they never get such information. While one Outside Limited Partner and relatives of two Outside Limited Partners are WRH clients and, as such, receive monthly statements of their portfolio positions, these statements only reflect investment decisions and trading activities that have already occurred in the previous month. Also, while the Reviewing Limited Partner receives WRH's general ledger for review on a quarterly basis on behalf of the other Outside Limited Partners, the general ledger contains no information concerning securities held in the clients' portfolios or the securities trading activities conducted on behalf of WRH clients.

The Staff has issued interpretive letters exempting the reporting of Personal Securities Transactions by advisory representatives in circumstances in which such advisory representatives had no prior knowledge or access to information about portfolio transactions of an investment adviser or affiliated investment adviser. For example, in Connecticut General Pension Services Inc. (publicly available June 21, 1982) ("Connecticut General"), the Staff advised Connecticut General that it would not recommend action against Connecticut if it failed to maintain Personal Securities Transactions reports for certain directors, officers and employees of Connecticut General who did not prepare, have duties relating to or obtain advance information regarding certain investment advice provided by an affiliated investment adviser with respect to specific investments by accounts used by Connecticut General.\* Also, in Prudential Insurance Co. of America (publicly available June 3, 1977) ("Prudential"), the Staff provided a similar no-action letter to Prudential, which was subject to the reporting requirements of Rule 204-2(a)(13) as opposed

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\* Connecticut General limited its own advice with respect to the accounts to advice regarding general types of investments of a similar nature, but not regarding specific securities.

to Rule 204-2(a)(12),\* with respect to certain officers and employees who allocated the funds of pension plan clients to different Prudential accounts, but who were not in a position to engage in scalping because they did not participate in or have access to information regarding the decisions with respect to the publicly-traded securities held by these accounts.\*\*

In addition to the lack of prior access to information concerning investment decisions described above, there is little practical risk of scalping abuse by the Outside Limited Partners in the high yield fixed income securities in which WRH specializes, even if they were to

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\* As mentioned above, the Commission views sub-paragraphs (12) and (13) of Rule 204-2(a) as complementary with the same primary purpose - to prevent scalping.

\*\* See also TransAmerica Advisors, Inc. (publicly available November 4, 1988), in which the Staff explained its modified position in The Boston Company, Inc. (publicly available April 27, 1987) ("TBC") as compared to Pioneering Management Corporation (publicly available February 27, 1985 ("Pioneering")). The Staff granted no-action relief in Pioneering for advisory representatives' transactions in shares of open-end funds, but limited this relief in TBC to "unaffiliated open-end funds," because of its concern that advisory representatives of an adviser managing a fund's portfolio securities, or of an investment adviser affiliated with that adviser, who have the ability to gain access to information about impending portfolio transactions involving securities for which there is an active secondary market, could misuse confidential information.

gain prior access to information concerning WRH's investment or trading decisions. Several factors reduce this risk. High yield fixed income securities are fundamentally different from equities in their susceptibility to scalping. The securities generally are denominated in units of \$1,000 face value. Except in the rare distressed or bankruptcy situation, these securities do not trade more than a few dollars above or below face value regardless of news about the issuing company. Instead, the most significant determinant of bond prices is prevailing interest rates. Unlike equities, it is highly unlikely that information concerning the investments of any single market participant will significantly impact the price of the securities when the information is finally disclosed. Thus, advance information about such investments is of little or no value.

Another factor is that the high yield fixed income securities market is dominated by institutions. Many issues are traded in compliance with Rule 144A of the Securities Act of 1933, as amended, in which individuals like the Outside Limited Partners cannot participate because they are not "qualified institutional buyers" under the Rule. In the high yield markets available to the public, the "round lot" size trade presently is roughly \$5 million. Even large public issues are thinly traded on a day to day basis by a

relatively small number of specialized brokers and the trades themselves are rarely reported on any organized exchange. Few individuals can trade at this level and the transactions costs of an "odd lot" size trade would more than offset any price change that could be expected based on advance information of investment decisions or trading activities of an investment adviser such as WRH. In other words, it is extremely difficult if not impossible for an individual to engage in scalping in the high yield debt market.

The Staff has issued no-action letters with respect to the reporting of Personal Securities Transactions by advisory representatives in circumstances in which there is an insufficient market effect from the securities investment recommendations made by the adviser. For example, in Connecticut General, the Staff noted not only the advisory representatives' lack of knowledge of the specific securities to be purchased or sold by the accounts for which such advisory representatives recommended general types of investments, but also the fact that "amounts being invested or disinvested by the accounts as a result of such recommendations are unlikely to have an effect upon the market prices of the securities purchased or sold sufficient

to permit such advisory representatives to engage in 'scalping'."

The Staff has noted that "where there is not a trading market for the securities recommended by the adviser and the possibility of 'scalping' by an 'advisory representative' does not exist, the purpose of Rule 204-2(a)(12) is not served by requiring the advisory representative to maintain a record of his or her personal securities transactions." See Connecticut General. Other letters to substantially similar effect with respect to the existence of a trading market are Massachusetts Financial Services Company, (publicly available October 6, 1992); Lipper Analytical Services, Inc. (publicly available June 5, 1990); TransAmerica Advisors, Inc. (publicly available November 4, 1988); Joshua, Lauren & Co. Inc. (publicly available October 11, 1988); and The Colonial Group, Inc. (publicly available March 10, 1988).

The Staff has granted relief from Rule 204-2(a)(12) on the basis that the potential for the abuse which the rule was designed to monitor and prevent was not present in particular situations. We submit that the same reasoning should apply to the situation of the Outside Limited Partners of WRH. Because the Outside Limited Partners do not participate in the management of WRH, do not

control its General Partners, do not participate in the formulation of securities investment decisions and have no information concerning such securities investment decisions, the opportunities for self-dealing, scalping and the other types of abuse targeted by Rule 204-2(a)(12) are not present in the context of transactions by WRH's Outside Limited Partners and the recordkeeping and reporting requirements of Rule 204-2(a)(12) should not be applied to them. Where, as in the case of the Outside Limited Partners, the advisory representative receives no information with respect to the securities investment decisions of the investment adviser, there is an effective barrier to scalping and other improper trading practices and the recordkeeping requirements of the rule are no longer necessary.

In addition, although WRH is organized as a limited partnership, the Outside Limited Partners are, in most respects, similar to shareholders of any investment adviser under the Act that is organized in corporate form. Unlike shareholders, however, who often enjoy the right to vote on the affairs of the corporation, the Outside Limited Partners have no ability whatsoever to control or bind WRH. Yet, unless a shareholder is also an officer, director or employee of or in a control relationship to the investment adviser, or an affiliated person of such controlling person

or an affiliated person of such affiliated person, such shareholder is not included in the definition of advisory representative in Rule 204-2(a)(12)(A) of the Act. However, as the term "partner" in Rule 204-2(a)(12)(A) of the Act may be broadly construed to encompass both general and limited partners, the Outside Limited Partners would be included in the definition of advisory representative.

We believe that the issue of access to trading information and the applicability of related record keeping requirements should not turn on the mere form of organization of the entity. If WRH were organized as a corporation rather than as a limited partnership and the Outside Limited Partners had corresponding economic interests in such corporation, they would not be subject to the requirements of Rule 204-2(a)(12) of the Act unless they were officers, directors, employees or controlling persons of such corporation. None of the Outside Limited Partners has powers analogous to officers or directors of corporations or is an employee of or in a control relationship to WRH. The Outside Limited Partners should not be deemed to be "advisory representatives" of WRH merely because they are partners with limited rights -- rights that as a matter of law prohibit them from taking part in the management and control of the limited partnership and by

contract limit them even further. Indeed, the Outside Limited Partners have fewer rights in respect of the affairs of WRH than common stockholders with equity investments of similar proportion in a corporation because common stockholders are entitled to vote in the election of directors.

C. Analogy to Investment Company Act of 1940

In another context (in this case relating to the substantive provisions of the Investment Company Act (the "ICA") and not only to a recordkeeping requirement such as Rule 204-2(a)(12) of the Act), the Staff has granted relief to persons with less than five percent limited partnership interests from the prohibitions against principal transactions under Section 17 of the Investment Company Act. Section 17(a) of the ICA provides in part that, except for certain transactions, it is unlawful for any "affiliated person" of a registered investment company or any affiliated person of such person to knowingly sell to such registered investment company any security or other property.

Similarly, Section 17(d) of the ICA makes it unlawful for any affiliated person of a registered investment company or any affiliated person of such person acting as principal to effect any transaction in which the registered investment company is a joint or a joint and

several participant with such person or persons in contravention of such rules and regulations as the Commission may prescribe. Rule 17d-1 of the ICA prohibits, with certain exceptions, an affiliated person of any registered investment company from participating in any "joint enterprise or other joint arrangement or profit sharing plan" with a registered investment company unless the Commission issues a formal order permitting such joint enterprise, arrangement or plan.

Section 2(a)(3) of the ICA defines, in relevant part, an "affiliated person" of another person to mean: "(A) any person directly or indirectly owning, controlling, or holding with power to vote, 5 per centum or more of the outstanding voting securities of such other person; . . . (C) any person directly or indirectly controlling, controlled by, or under common control with such other person; (D) any officer, director, partner, copartner, or employee of such other person; (E) if such person is an investment company, any investment adviser thereof . . . ." The definition of "affiliated person" in Section 2(a)(3) of the ICA is similar to the definition of "advisory representative" in Rule 204-2(a)(12)(A) of the Act in that it also provides for differential treatment of limited partners and shareholders - limited partners are always deemed affiliated persons

whereas shareholders must own five percent or more of the outstanding voting securities of such other person.

The Commission has issued a number of orders pursuant to Section 6(c) exempting from the Section 2(a)(3) definition of affiliated persons limited partners of investment companies of investment advisers thereof who hold less than five of the interests in such entities organized as limited partnerships. In ICA cases, applicants for an exemption from the Section 2(a)(3) definition have made contentions analogous to those made by us in this letter arguing that the question of affiliation and the applicability of related prohibitions should not turn on the mere form of organization of the entity, that limited partners should not be deemed to be "affiliated persons" of a registered investment company merely because they are partners with limited rights -- rights that as a matter of law prohibit them from taking part in the management and control of the limited partnership and which as a matter of contract are even more restricted -- and that an exemption would place transactions entered into by holders of less than five percent of the limited partner interests of an investment company on a footing more equal with investments by holders of less than five percent of the shares of affiliated persons of such investment company.

Since 1976, the Commission has issued over forty orders providing essentially this type of relief, thus putting persons with less than five percent limited partnership interests on equal footing with their shareholder counterparts. Among the more recent letters, see Technology Funding Medical Partners I, L.P., Investment Company Release No. 19183 (December 28, 1992) (less than five percent limited partners treated like less than five percent shareholders for purposes of Section 2(a)(3) of the ICA); Previously Owned Partnerships Income Fund-92, Investment Company Release No. 19099 (November 16, 1992) (same); Community Investment Partners II, L.P., Investment Company Release No. 19004 (October 6, 1992) (same); The Goldman Sachs Group, L.P., Investment Company Release No. 18994 (October 1, 1992) (same); Panther Partners, L.P., Investment Company Release No. 18213 (June 25, 1991) (same); Renaissance Capital Partners II, Ltd., Investment Company Release No. 18312 (September 13, 1991) (same); Renaissance Capital Partners II, Investment Company Release No. 18174 (May 30, 1991) (same); and Equus Investments II, L.P., Investment Company Release No. 18011 (February 20, 1991) (same).

Indeed, the exemption for limited partners with less than five percent partnership interests from the

definition of affiliated person in Section 2(a)(3) of the ICA had become so routine and the force of the arguments in support thereof so compelling that the Commission adopted, effective September 30, 1993, Rule 2a3-1 of the ICA, which excepts from the definition of affiliated person in Section 2(a)(3) those limited partners of limited partnership investment companies that are affiliated persons solely because they are limited partners. See Investment Company General Partners Not Deemed Interested Persons; Investment Company Limited Partners Not Deemed Affiliated Persons, Investment Company Release No. 19658 (August 25, 1993), 58 FR 45834 (August 31, 1993) (adopting release). Rule 2a3-1 of the ICA was proposed to codify the prior Commission orders, thus giving the limited partners the same treatment as shareholders for purposes of the affiliated person definition, i.e., if a limited partner directly or indirectly owns, controls or holds with the power to vote, less than five percent of the outstanding voting interests of the limited partnership investment company, the investment adviser, or the principal underwriter, then the limited partner would not be an affiliated person of such persons under Section 2(a)(3)(A) of the ICA. This permits a limited partnership investment company to engage in transactions with its limited partners and their affiliated

persons to the same extent as if the investment company were organized as a corporation, thereby making it easier for investment companies desiring to use the limited partnership form to do so.

In its proposing release, the Commission, after recognizing the disparity in treatment between limited partners of a limited partnership investment company and shareholders of a corporate investment company, stated that:

There appears to be no reason to treat limited partners and shareholders of an investment company differently under the affiliated transactions provisions of the [ICA]. Limited partners, like shareholders, are passive investors in the investment company, and where neither type of investor owns more than five percent of the voting securities, there is little, if any, potential for overreaching.\*

We believe that the exemptions to the Section 2(a)(3) definition of affiliated persons granted to the less than five percent limited partners of limited partnership investment companies, now codified in Rule 2a3-1 of the ICA, are analogous to the relief we request from the Rule 204-2(a)(12) of the Act definition of advisory representatives and provide support for the requested relief.

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\* Investment Company General Partners Not Deemed Interested Persons; Investment Company Limited Partners Not Deemed Affiliated Persons, Investment Company Release No. 18868 (July 28, 1992), 58 FR 34726 (August 6, 1992) (proposing release).

D. Undertakings

As a condition to the relief requested hereby from the record keeping requirements of WRH pursuant to Rule 204-2(a)(12) of the Act with respect to the Personal Securities Transactions of the Outside Limited Partners of WRH, WRH will undertake to continue to maintain the records required pursuant to such Rule with respect to the Personal Securities Transactions of the General Partners and the Employee Limited Partners.

Pursuant to these record keeping requirements, WRH will maintain and enforce its written policies and procedures that involve regular reporting and review of Personal Securities Transactions. Among other things, WRH has policies that require: (i) the Employee Limited Partners to submit prior written requests for authorizations to trade in their personal accounts, (ii) approval from a designated compliance officer for any Personal Securities Transactions prior to a trade, (iii) the disclosure to WRH of all brokerage accounts maintained by the General Partners and Employee Limited Partners, (iv) the Employee Limited Partners to provide WRH with signed authorizations for the broker to provide WRH with copies of all trade confirmations, monthly statements and year-end summaries (if such summaries are produced), (v) the review by a designated

senior compliance officer of WRH of such confirmations, statements and summaries, (vi) the maintenance by WRH of complete files of such confirmations, statements and summaries and (vii) each of the General Partners and the Employee Limited Partners to acknowledge in writing that he has read and understands the policies and procedures of WRH concerning Personal Securities Transactions and to agree to comply with them. In addition, WRH will continuously monitor these policies and procedures to ensure their efficacy. Finally, although WRH does not have an internal education program, employees are regularly required to attend seminars for investment advisers which include discussions of conflicts of interest that may be present in particular situations and give guidance as to what types of information present the potential for abuse.

As a further condition to the relief requested hereby, WRH will undertake to continue to exclude the Outside Limited Partners (including the retiring Employee Limited Partner) from the process of formulating and executing WRH's securities investment decisions and from receiving any trading information. Pursuant to such undertaking, WRH will continue to maintain and enforce policies and procedures reasonably designed to prevent the

Outside Limited Partners (including the retiring Employee Limited Partner) from obtaining trading information.

The offices of WRH allow no access to the public and are secured by key pad entry and alarm systems. The portfolio position and trading activity records of WRH are maintained only in the offices of WRH, in locked file cabinets and restricted computer files.

During the last five years, the Reviewing Limited Partner has been to WRH's offices only twice, and then only with prior appointments. The other Outside Limited Partners have never been to WRH's offices and no Outside Limited Partner has ever had access to WRH's portfolio position and trading activity records.

WRH will undertake to continue limiting access by the Outside Limited Partners to WRH's offices. While it is unlikely that there will be any future meetings with the Reviewing Limited Partner or the other Outside Limited Partners, WRH undertakes that any such meetings will be conducted off site. WRH's General Partners and employees will continue to refrain from discussing portfolio positions or trading activities with the Outside Limited Partners at these meetings or otherwise. WRH will continue to keep its portfolio position and trading activity records secure and will not allow any access to the records by the Outside

Limited Partners. The Outside Limited Partners, other than the Reviewing Limited Partner, will continue to receive only their quarterly distributions of profits.

As a further condition to the relief requested hereby, WRH will undertake to continue to provide the Reviewing Limited Partner with only the type of information he has previously received: the general ledger, which ledger contains the financial records of WRH and also includes a list of its investment management clients and the fees received from each such client, but which contains no information concerning securities held in the clients' portfolios or the securities trading activities of WRH.

### III. Conclusion

In light of the foregoing, we request that the Staff advise us that the Outside Limited Partners should not be treated as "advisory representatives" pursuant to Rule 204-2(a)(12) solely because they are limited partners of WRH and that therefore the Staff would not recommend enforcement action to the Commission if WRH does not maintain the records of Personal Securities Transactions of the Outside Limited Partners as is required of advisory representatives pursuant to Rule 204-2(a)(12).

If you have any questions with respect to the foregoing or require further information with respect to

this request, please call the undersigned (212-558-4854) or  
John Baumgardner (212-558-3866) or Donald Crawshaw  
(212-558-4016) of this office.

Very truly yours,

A handwritten signature in black ink, appearing to read "Adam Kupitz", with a long horizontal flourish extending to the right.

Adam M. Kupitz